

Translation from original in Russian language



OJSC Karazhanbasmunai

Financial Statements

*Years ended December 31, 2002 and 2001
with Independent Auditors' Report*

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Ernst & Young

273 Furmanova St.
Almaty Kazakhstan 480099
Phone: 7(3272) 585 960
7(3272) 585 969
Fax: 7(3272) 585 961

Эрнст энд Янг

273 ул. Фурманова
Алматы Казахстан, 480099
Телефон: 7(3272) 585 960
7(3272) 585 969
Факс: 7(3272) 585 961

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Report of Independent Auditors

To the Shareholders of Open Joint Stock Company Karazhanbasmunai:

We have audited the accompanying balance sheet of Open Joint Stock Company Karazhanbasmunai ("the Company") as at December 31, 2002 and the related statements of income, cash flows and changes in equity for the year then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audit. The financial statements of the Company as of December 31, 2001, were audited by other auditors who have ceased operations and whose report dated February 14, 2002 expressed an unqualified opinion on those statements.

We conducted our audit in accordance with Kazakhstani Standards on Auditing. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statements presentation. We believe that our audit provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above, present fairly, in all material respects, the financial position of the Company as at December 31, 2002 and results of its operations and cash flows for the year then ended in accordance with Kazakhstani Accounting Standards.



Aisulu Narbaeva, General Director

Almaty

February 26, 2003



BALANCE SHEETS

<i>In thousands of Kazakhstani tenge</i>	Note	December 31,	
		2002	2001
Current assets			
Cash and cash equivalents	3	2,457,593	190,801
Trade accounts receivable	4	4,961,002	860,414
Amounts due from Parent	5	1,590,629	612,875
Inventories	6	2,603,897	2,150,578
Prepayment for taxes	7	–	980,143
VAT receivable		947,517	1,249,261
Other current assets, net	8	1,650,940	1,250,504
		14,211,578	7,294,576
Non-current assets			
Property, plant and equipment, net	9	25,726,149	21,940,683
Intangible assets, net	10	531,382	454,779
Long-term financial investments	11	1,556,000	1,502,000
Other non-current assets	12	519,719	147,878
		28,333,250	24,045,340
Total assets		42,544,828	31,339,916
Current liabilities			
Current portion of long - term debt	16	6,976,570	6,340,933
Bond obligations	16	3,112,000	–
Trade accounts payable	13	1,611,197	1,063,935
Taxes payable	14	899,298	94,348
Accrued liabilities and other payables	15	389,913	302,253
		12,988,978	7,801,469
Non current liabilities			
Long - term debt	16	8,781,307	8,849,599
Deferred tax liability	17	5,897,461	4,491,304
Other long-term liabilities	18	82,312	–
Future site restoration and abandonment reserve	19	615,659	412,112
		15,376,739	13,753,015
Shareholders' equity			
Share capital	20	2,161,251	2,161,251
Unpaid capital		(189)	(189)
Reserve fund		324,188	324,188
Revaluation reserve		5,415,201	6,017,849
Retained earnings		6,278,660	1,282,333
		14,179,111	9,785,432
Total liabilities and shareholders' equity		42,544,828	31,339,916

The accounting policies and explanatory notes on pages 6 through 20 form an integral part of these financial statements.

First Vice President OJSC Karazhanbasmunai

M. Long

Chief Accountant OJSC Karazhanbasmunai

Zoya Chistova

STATEMENTS OF INCOME

<i>In thousands of Kazakhstani tenge</i>	For the years ended December 31,		
	Note	2002	2001
Revenue	21	34,754,442	17,584,246
Cost of sales	22	(6,317,501)	(4,514,336)
Gross profit		28,436,941	13,069,910
Expenses			
Transportation expenses		(5,009,451)	(1,208,574)
Selling, general and administrative expenses	23	(4,584,349)	(3,677,470)
Provision for site restoration and abandonment		(203,547)	(194,834)
Depreciation, depletion and amortization		(1,449,349)	(490,380)
Profit from operations		17,190,245	7,498,652
Other expenses			
Finance costs		(2,556,576)	(1,325,955)
Foreign exchange loss, net		(349,892)	(283,664)
Other non-operating income (expense), net		42,479	(57,718)
Profit before income taxes		14,326,256	5,831,315
Income taxes	17	(5,141,327)	(1,888,489)
Net profit		9,184,929	3,942,826

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First Vice President OJSC Karazhanbasmunai

M. Long

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Zoya Chistova

STATEMENTS OF CASH FLOWS

<i>In thousands of Kazakhstani tenge</i>	For the years ended December 31,		
	Note	2002	2001
Cash flows from operating activities:			
Profit before taxation		14,326,256	5,831,315
Adjustments for:			
Depreciation, depletion and amortization		1,449,349	490,380
Loss on disposal of property, plant and equipment		216,971	103,774
Unrealized foreign exchange (gain)/loss (net)		54,000	–
Production bonus		82,312	–
Provisions for bad debt and other current assets		33,870	68,852
Provision for future site restoration and abandonment		203,547	194,834
Operating profit before changes in working capital		16,366,305	6,689,155
Increase in trade accounts receivable		(4,100,588)	(860,414)
Increase in inventories		(453,319)	(1,462,749)
(Increase)/decrease in prepayment for taxes		183,292	(322,066)
(Increase)/decrease in VAT receivable		301,744	(699,520)
Increase in other assets		(689,811)	(1,220,215)
Increase in trade accounts payable		547,262	446,094
Decrease in advances received from customers		–	(1,235,786)
Increase/(decrease) in taxes payable		308,629	(50,640)
Increase/(decrease) in interest payable		(41)	10,795
Increase in accrued liabilities and other payables		87,701	148,318
Cash generated from operations		12,551,174	1,442,972
Income taxes paid		(2,441,998)	(581,143)
Net cash flows from operating activities		10,109,176	861,829
Cash flows from investing activities:			
Purchase of property, plant and equipment and intangible assets		(5,436,504)	(7,535,383)
Proceeds from disposal of property, plant and equipment		2,208	115,115
Purchase of Investments		–	(1,502,000)
Long term advances		(116,336)	(93,435)
Net cash flows used in investing activities		(5,550,632)	(9,015,703)
Cash flows from financing activities:			
Bonds issuance proceeds		–	2,106,005
Increase in long-term loans		3,571,345	8,359,472
Dividends paid	20	(4,885,343)	(3,738,769)
Financing from (to) Parent		(977,754)	1,065,727
Net cash flows from (used in) financing activities		(2,291,752)	7,792,435
Net increase/(decrease) in cash and cash equivalents		2,266,792	(361,439)
Cash and cash equivalents at the beginning of period	3	190,801	552,240
Cash and cash equivalents at the end of period	3	2,457,593	190,801

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First Vice President OJSC Karazhanbasmunai

M. Long

Chief Accountant OJSC Karazhanbasmunai

Zoya Chistova

STATEMENTS OF CHANGES IN EQUITY

<i>In thousands of Kazakhstani tenge</i>	Share Capital	Additional Unpaid Capital	Reserve Capital	Revaluation Reserve	Retained Earnings	Total
As at December 31, 2000	2,161,251	(149)	324,188	628,876	1,025,435	4,139,601
Revaluation of PP&E, net of the deferred tax effect	–	–	–	5,441,814	–	5,441,814
Equity adjustment	–	(40)	–	–	–	(40)
Amortization of revaluation reserve	–	–	–	(52,841)	52,841	–
Net income for the year	–	–	–	–	3,942,826	3,942,826
Dividends	–	–	–	–	(3,738,769)	(3,738,769)
As at December 31, 2001	2,161,251	(189)	324,188	6,017,849	1,282,333	9,785,432
Revaluation adjustment	–	–	–	94,093	–	94,093
Disposal of fixed assets	–	–	–	(158,130)	158,130	–
Amortization of revaluation reserve	–	–	–	(538,611)	538,611	–
Net income for the year	–	–	–	–	9,184,929	9,184,929
Dividends	–	–	–	–	(4,885,343)	(4,885,343)
As at December 31, 2002	2,161,251	(189)	324,188	5,415,201	6,278,660	14,179,111

The accounting policies and explanatory notes on pages 6 through 20 form an integral part of these financial statements.

First Vice President OJSC
Karazhanbasmunai

M. Long

Chief Accountant OJSC
Karazhanbasmunai

Zoya Chistova

NOTES TO THE FINANCIAL STATEMENTS

1. GENERAL

The Experimental Oil and Gas Extracting Department of the Republic of Kazakhstan (“NGDU Karazhanbasneft”) was established in 1986 as an independent enterprise. NGDU Karazhanbasneft was subsequently restructured to form the Open Joint Stock Company Karazhanbasmunai (the “Company”). The Company was registered in Mangistau oblast, Western Kazakhstan, on April 23, 1993. The majority of the Company’s shares are owned by Nations Energy Company Ltd. (“Nations Energy” or “Parent”). Nations Energy Company Ltd. is a company incorporated in Alberta, Canada.

The Company is engaged in the exploration, production and sale of oil from the Karazhanbas field in Western Kazakhstan. The Company signed a subsoil use contract with the Government of Kazakhstan on May 23, 1997 and has a license for hydrocarbon exploration and production (the “License”) on Karazhanbas field that is valid until June 7, 2020. According to the report of independent petroleum engineers Miller & Lents, Ltd., as of January 1, 2002, the Company’s total proved oil reserves were approximately 337 million barrels.

The Company is located in Aktau, Mangistau oblast, Republic of Kazakhstan (or “Kazakhstan”) and has a branch in Almaty.

As of December 31, 2002 and December 31, 2001 the Company employed 2,453 and 2,387 employees, respectively.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Preparation

The accompanying financial statements have been prepared under the historical cost basis, as modified by the revaluation of fixed assets, and in conformity with Kazakhstani Accounting Standards (“KAS”).

The Company is required by accounting and tax legislation in Kazakhstan to maintain accounting records and draw up financial statements in Kazakhstani tenge (“tenge”).

The preparation of financial statements in accordance with KAS requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses, and the disclosure of contingent liabilities. Actual results may differ from management’s estimates made at the time of preparing these financial statements. These financial statements have been prepared in accordance with KAS on a going concern basis, which assumes the realization of assets and discharge of liabilities in the normal course of business within the foreseeable future.

Reclassification of Prior Year Balances

Certain reclassifications have been made within the 2001 financial statements to be consistent with the 2002 presentation. These reclassifications have not changed either net profit or equity for the prior year.

Foreign Currency Translation

Monetary assets and liabilities that are denominated in currencies other than tenge, are translated at exchange rates prevailing at the balance sheet date. Revenues, costs, non-monetary assets and liabilities and capital are translated at historical exchange rates prevailing on the transaction date. Exchange gains and losses arising from translation of monetary assets and liabilities that are not denominated in tenge are credited or charged to operations.

NOTES TO THE FINANCIAL STATEMENTS (continued)

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Oil and Gas Reserves

The Company uses the reserve estimates provided by independent petroleum engineers to assess the oil and gas reserves. These reserve quantities are used as the basis for calculating the units of production depreciation within the financial statements.

Oil and Gas Properties

The Company follows the method of accounting for its oil exploration, development and production activities as described in KAS 20 "Accounting for Oil and Gas Producing Companies".

At present, the Company does not have any capitalized field acquisition costs. Should they be incurred in the future, field acquisition costs related to properties held for oil and gas production will be capitalized when incurred. Unproven properties with acquisition costs, which are individually significant, will be assessed on a property-by-property basis, and a loss recognized by provision of a valuation allowance, when the assessment indicates impairment in value. Unproven properties with acquisition costs, which are not individually significant, will generally be aggregated and the portion of such costs estimated to be non-productive based on historical experience, will be amortized on an average holding period basis.

Exploratory costs, excluding the costs of exploratory wells, are expensed as incurred. Costs of drilling exploratory wells, including stratigraphic test wells, are capitalized pending determination whether such wells have found proved reserves, which justify commercial development. If such reserves are not found, the drilling costs are charged to exploratory expenses. Intangible drilling costs applicable to productive wells and to development dry holes, as well as tangible equipment costs and costs of injection wells related to development of oil and gas reserves are capitalized.

The Company currently operates a field with proven reserves. Costs incurred in development of proven reserves are capitalized.

The Company reviews its oil and gas properties whenever events and circumstances indicate a decline in the recoverability of their carrying value. As of December 31, 2002, the Company reviewed its oil and gas properties carrying value for possible impairment. The Company compared the expected undiscounted future cash flows from proven reserves to the carrying amount to determine if the carrying amount was recoverable and determined that no impairment was required.

Depreciation and depletion of capitalized costs of proven oil and gas properties is calculated using the unit-of-production method in accordance with KAS 20.

Gains or losses on disposal of oil and gas properties are booked to current year income and expense.

Property, plant and equipment

Property, plant and equipment are stated at historical cost or revalued amount less accumulated depreciation. Depreciation of non-production property, plant and equipment is calculated on a straight-line basis over the estimated useful life of the assets as presented below:

Buildings and constructions.....	20 years
Machinery and equipment.....	8-30 years
Vehicles.....	5 years
Other.....	10 years

NOTES TO THE FINANCIAL STATEMENTS (continued)

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Property, plant and equipment (continued)

Repair and maintenance costs are charged to income as incurred. Renewals and betterment are capitalized. When assets are sold, retired or otherwise disposed of, the applicable costs and reserves are removed from the accounts and the resulting gain or loss is recognized.

Construction in progress represents capital construction of projects not yet completed as well as prepayments made to contractors related to construction projects and interest on bank loans used on these projects. When these assets begin to be used in production they are transferred to the appropriate asset class. Since construction in progress is not used in production, these assets are not subject to depreciation.

Intangible Assets

Intangible assets include software, re-registration expenses and License fees. These are stated at original cost and amortized on a straight-line basis over five years. Also included is the cost of oil field development program and seismic maps that will be used by the Company over the production period. These costs are amortized based on unit-of-production method.

Cash and Cash Equivalents

Cash on hand and in banks and bank deposits, which are held to maturity, are carried at cost.

Cash and cash equivalents are defined as cash on hand, demand deposits and short-term and highly liquid investments readily convertible to known amount of cash and subject to insignificant risk of changes in value.

Trade and Other Receivables

Trade receivables are recognized and carried at original invoice amount less an allowance for any uncollectible amounts. An estimate for doubtful debts is made when collection on the full amount is no longer probable. Bad debts are written off when identified.

Inventories

Inventories are stated at the lower of cost or net realizable value. Cost of materials and crude oil is determined using the FIFO method. Crude oil inventory consists primarily of oil in pipelines and tanks. The cost of crude oil inventory includes all direct costs.

Loans and Borrowings

Loans and borrowings are recognized at cost, being the fair value of the consideration received.

Trade and Other Payables

Liabilities for trade and other amounts payable are carried at cost which is the fair value of the consideration to be paid in the future for goods and services received, whether or not billed to the Company.

Abandonment and Site Restoration Costs

Estimated site restoration costs are provided for on a monthly basis over the duration of the Company's License to develop the Karazhanbas field. Costs are based on engineering estimates of the anticipated method and extent of the site restoration, in accordance with current Kazakhstani legislation, industry practices and costs. Provision is made for estimated site restoration costs that are expected to be incurred.

NOTES TO THE FINANCIAL STATEMENTS (continued)

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Provisions

Provisions are recognized when the Company has a present obligation (legal or constructive) as a result of a past event, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation.

Retirement Benefit Obligation

The Company pays certain social insurance taxes to the tax authorities, which represent its contribution to the post retirement benefits of its employees. The Company has no other program or obligation for payment of post retirement benefits to its local and expatriate employees.

The Company also withholds and contributes 10% from the salary of its employees as the employees' contribution to their designated pension funds. Under the legislation, employees are responsible for their retirement benefits and the Company has no present or future obligation to pay its employees upon their retirement.

Revenue Recognition

Revenue is recognized when it is probable that the economic benefits associated with the transaction will flow to the Company and the amount of revenue can be reliably measured.

Revenue from the sale of crude oil is recognized when delivery has taken place and the significant risks and rewards of ownership of the crude oil have passed to the buyer and the amount of revenue can be measured reliably. Sales income does not include indirect taxes (excises, VAT, and royalties) and is stated at the net amount (after discounts and pipeline losses). Expenses and losses are recognized when incurred.

Deferred Taxes

Deferred income tax is provided, using the liability method, on all timing differences for the year between taxable income and accounting income reported for financial statement purposes.

Income Taxes

The statutory corporate income tax is currently 30%. Entities are obliged to make monthly advance corporate income tax payments.

Dividends and Reserve Capital

Dividends payable are recognized as an appropriation of net profit in the period when declared. Reserve Capital represents 15% of the Company's authorized capital as required by the Company's charter, to cover future losses and it is not distributable.

Long-Term Financial Investments

All investments are initially recognized at cost, being the fair value of the consideration given and including acquisition charges associated with the investment. After initial recognition, investments, which are classified as "available-for-sale" are measured at fair value.

NOTES TO THE FINANCIAL STATEMENTS (continued)

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Related parties

Related parties include the Company's shareholders, investee and other companies that either could execute control over the Company or have significant influence on the financial and operating decision making process of the Company.

Revaluation Reserve

The recorded costs for property plant and equipment acquired before 1996 include the effect of revaluations made during the years 1993 through 1996 in accordance with indices published by the Ministry of Finance. Such revaluations were mandatory. The revaluation adjustments were recorded within the revaluation reserve in shareholders' equity, a significant portion of which was transferred to share capital prior to the Company's privatization. In 2002, the Company engaged an independent appraisal firm to opine on the fair market value of the Company's property, plant and equipment inclusive of oil properties. The resulting revaluation was reflected in the Company's books with effect as of December 31, 2001. Increases in carrying values of individual assets were recorded as an increase to the revaluation reserve. The revaluation reserve is realized in proportion with the use of the underlying assets. The amount of the revaluation reserve realized is the difference between depreciation/depletion based on the revalued carrying amount of the asset and depreciation based on the asset's original cost. Such amounts are therefore transferred from revaluation surplus to retained earnings each period. Upon the disposal of a revalued asset, the relevant remaining portion of the revaluation reserve is realized in respect of previous valuations released from the asset's revaluation reserve directly to retained earnings. This realization of revaluation reserve is shown in the statement of changes in equity as disposals of fixed assets.

Borrowing Costs

Borrowing costs are recognized as expenses in the period in which they are incurred. Any interest costs relating to capital work in progress is capitalized and then appropriately amortized.

The Company capitalizes costs relating to the fees incurred in connection with obtaining loan facilities which are amortized over the life of the maturity.

3. CASH AND CASH EQUIVALENTS

As of December 31, 2002 and 2001 cash and cash equivalents represented mainly current accounts and time deposits with Kazakh banks.

4. TRADE ACCOUNTS RECEIVABLE

As of December 31, 2002 and 2001 trade accounts receivable represented amounts due from customers for sales of oil.

5. AMOUNTS DUE FROM PARENT

As of December 31, 2002 and 2001 amounts due from Parent comprised:

<i>In thousands of Kazakhstani tenge</i>	2002	2001
Short-term financing	2,316,874	15,582
Management fees (payable) prepaid	(726,245)	597,293
	1,590,629	612,875

NOTES TO THE FINANCIAL STATEMENTS (continued)**5. AMOUNTS DUE FROM PARENT (continued)**

The Company provides short-term financing to Nations Energy. The short-term financing are non-interest bearing, revolving and repaid by the Parent within 120 days. The receivable balance due from the Parent is either settled in cash or is offset against other payable balances due to the Parent.

In March 2000 the Company signed an agreement with Nations Energy, under which Nations Energy renders management services, including administration, consulting, marketing and other services (“the Management Agreement”). For the year 2000 and thereafter the Management Agreement calls for a monthly management fee of US\$ 250,000 (38,083 thousand tenge) plus costs for third party consulting charges, materials and corporate general and administrative expenses of Nations Energy, incurred during fulfillment of its duties under the Management Agreement.

6. INVENTORIES

As of December 31, 2002 and 2001 inventories comprised:

<i>In thousands of Kazakhstani tenge</i>	2002	2001
Spare parts and materials	2,226,496	1,738,318
Crude oil	123,577	252,366
Fuel	66,368	31,608
Other	187,456	128,286
	2,603,897	2,150,578

7. PREPAYMENT FOR TAXES

As of December 31, 2002 and 2001 prepayment for taxes comprised:

<i>In thousands of Kazakhstani tenge</i>	2002	2001
Withholding tax	–	42,408
Excise tax	–	140,256
Corporate Income tax	–	796,851
Other	–	628
	–	980,143

8. OTHER CURRENT ASSETS, NET

As of December 31, 2002 and 2001 other current assets comprised:

<i>In thousands of Kazakhstani tenge</i>	2002	2001
KBC loan fee	353,217	632,736
Advances to suppliers	1,256,018	615,386
Receivable from personnel	39,242	58,889
Deferred expenses	86,699	33,880
Less: reserve for possible non-performance	(84,236)	(90,387)
	1,650,940	1,250,504

The Company incurred certain fees in connection with obtaining the Loan facilities from KBC Bank N.V. (see Note 16). The fee costs are capitalized and amortized over the life of the maturity.

Advances made to suppliers comprise of prepayments for inventory and services utilized in the normal course of business.

NOTES TO THE FINANCIAL STATEMENTS (continued)**9. PROPERTY, PLANT AND EQUIPMENT, NET**

As of December 31, 2002 property, plant and equipment comprised:

<i>In thousands of Kazakhstani tenge</i>	Oil & Gas Properties	Buildings & Premises	Machinery & equipment	Transportation	Other	Construction-in-progress	Total
Balance at January 1, 2002, net of accumulated depreciation	16,735,438	470,492	1,050,321	1,159,689	153,190	2,371,553	21,940,683
Additions	572,120	8,666	45,718	189,906	58,432	4,482,735	5,357,577
Transfers	5,120,591	5,449	436	2,249	4,279	(5,133,004)	–
Disposals	(211,084)	(8,786)	(28,316)	(38,448)	560	–	(286,074)
Depreciation charge	(1,079,622)	(33,562)	(130,285)	(190,157)	(15,607)	–	(1,449,233)
Depreciation on disposals	23,124	461	17,836	27,688	(6)	–	69,103
Reclassifications and adjustments	735,231	(84,408)	(586,566)	32,165	(5,754)	3,425	94,093
Balance at December 31, 2002, net of accumulated depreciation	21,895,798	358,312	369,144	1,183,092	195,094	1,724,709	25,726,149
At cost	17,409,315	450,318	619,325	1,344,763	211,020	1,724,709	21,759,450
Valued by Independent Appraiser	7,478,504	32,661	27,113	326,702	12,357	–	7,877,337
Accumulated depreciation	(2,992,021)	(124,667)	(277,294)	(488,373)	(28,283)	–	(3,910,638)
Net carrying amount	21,895,798	358,312	369,144	1,183,092	195,094	1,724,709	25,726,149

Interest expense of 238,763 thousand tenge incurred in 2002 was capitalized as part of additions to construction-in-progress for the year (2001:226,864 thousand tenge).

The Company used the quantities of proved developed reserves of 198.5 million barrels, estimated by independent petroleum engineers as of January 1, 2002, as a base for calculation of depletion, depreciation and amortization costs of oil and gas properties for the year.

As discussed in Note 2, in 2002 the Company engaged an independent appraisal firm to opine on the fair market value of the Company's property, plant and equipment inclusive of oil and gas properties as of December 31, 2001. The resulting revaluation in the amount of 7,877 million Tenge was reflected in the Company's books with effect as of December 31, 2001. Increases in the carrying values of individual assets were recorded as an increase to the revaluation reserve.

The Company made certain adjustments in 2002 relating to appropriate reallocation of revaluation surplus between the different categories of assets. These adjustments have been included within the "Reclassification and adjustments" category.

NOTES TO THE FINANCIAL STATEMENTS (continued)**10. INTANGIBLE ASSETS**

As of December 31, 2002 intangible assets comprised:

<i>In thousands of Kazakhstani tenge</i>	Exploration		
	Costs	Other	Total
Balance at January 1, 2002, net of accumulated amortization	416,595	38,184	454,779
Additions	–	108,590	108,590
Amortization for the year	(22,534)	(9,453)	(31,987)
Balance at December 31, 2002, net of accumulated amortization	394,061	137,321	531,382
At cost	423,144	158,064	581,208
Accumulated amortization	(29,083)	(20,743)	(49,826)
Net carrying amount	394,061	137,321	531,382

11. LONG-TERM FINANCIAL INVESTMENTS

As of December 31, 2002 and December 31, 2001 long-term financial investment represents US\$ 10 million (1,556,000 and 1,502,000 thousand tenge respectively) invested into a previously unrelated oil and gas company with operations in Azerbaijan. The Company purchased 8% ownership interest in the share capital of the investee during 2001.

12. OTHER NON-CURRENT ASSETS

As of December 31, 2002 and 2001 other non-current assets comprised:

<i>In thousands of Kazakhstani tenge</i>	2002	2001
Long-term portion of KBC loan fee (see Note 8)	311,826	56,321
Advances for equipment	207,893	91,557
	519,719	147,878

13. TRADE ACCOUNTS PAYABLE

As of December 31, 2002 and 2001 trade accounts payable comprised amounts due to suppliers for goods and services incurred during regular business activities.

Trade accounts payable as of December 31, 2002 includes a payable balance of 331 million tenge due to Tulpar Munai Service, a Parent's subsidiary.

14. TAXES PAYABLE

As of December 31, 2002 and 2001 taxes payable comprised:

<i>In thousands of Kazakhstani tenge</i>	2002	2001
Corporate income tax	496,321	–
Royalties	100,170	32,093
Withholding income tax	178,315	–
Social tax	40,250	29,488
Individual income tax	25,958	28,261
Other	58,284	4,506
	899,298	94,348

NOTES TO THE FINANCIAL STATEMENTS (continued)**15. ACCRUED LIABILITIES AND OTHER PAYABLES**

As of December 31, 2002 and 2001 accrued liabilities and other payables comprised:

<i>In thousands of Kazakhstani tenge</i>	2002	2001
Salaries and related payables	334,078	172,210
Pension fund	22,666	21,780
Interest on loans	13,624	8,711
Bonds interest payable	8,585	13,539
Dividends payable	8,809	86,013
Other	2,151	–
	389,913	302,253

16. LONG-TERM DEBT

As of December 31, 2002 and 2001 long-term debt comprised:

<i>In thousands of Kazakhstani tenge</i>	Date of Issue	Maturity Date	Annual Interest rate	Original Currency	2002	2001
Kazkommerzbank loan	Jun 19, 2000	May 19, 2005	14%	USD	2,039,144	2,036,252
Halyk Savings Bank loan	Jun 19, 2000	Jun 22, 2005	14%	USD	1,400,400	1,351,800
Bank TuranAlem loan	May 7, 2001	May 30, 2004	14%	USD	2,204,333	3,629,833
KBC Bank N.V. #1	Jul 18, 2001	Jan 27, 2003	LIBOR+4.5%	USD	–	5,168,647
KBC Bank N.V. #2	June 29, 2002	June 30, 2005	LIBOR+5%	USD	10,114,000	–
Bond obligations	Dec 2000	Dec 2003	11%	USD	3,112,000	3,004,000
Less: current portion of long term debt					(6,976,570)	(6,340,933)
Less: current portion of bond obligations					(3,112,000)	–
Long-term debt, net of current portion					8,781,307	8,849,599

The loan from Kazommerzbank is collateralized by equipment in the amount of US\$10 million and inventory for approximately the same amount. Interest is calculated at 14% per annum. The loan matures in May 2005.

The loan from Halyk Savings Bank is secured by the Company's assets in the amount of 1,981 million tenge. Interest is calculated at 14% per annum. The loan matures in June 2005.

The Company pledged assets of US\$15 million (approximately 2,334 million tenge) and future cash receipts from crude oil sales amounting to US\$ 50 million (approximately 7,780 million tenge) annually during two years to secure the loan from Bank TuranAlem. Interest is calculated at 14% per annum. The loan matures in May 2004.

In July 2001, the Company obtained a US \$45 million (approximately 6,683 million tenge) credit facility from KBC Bank N.V. ("KBC") at LIBOR plus 4.5% per annum. The loan matures in January 2003 and is to be repaid by equal monthly installments of US \$2.65 million (approximately 394 million tenge) starting in September 2001 by automatic withdrawals from the Company's bank account with KBC. In July 2002 the Company fully repaid the total outstanding debt due to KBC under this credit facility.

In January 2002 the Company obtained another US \$20 million (approximately 3,004 million tenge) credit facility from KBC at LIBOR plus 2.9% per annum, which provides for a 6-month grace period after which it has to be repaid by equal monthly installments over 12 months. In July 2002 the Company fully repaid the total outstanding debt due to KBC under this credit facility.

NOTES TO THE FINANCIAL STATEMENTS (continued)**16. LONG-TERM DEBT (continued)**

In June 2002, the Company entered into new US\$ 65 million facility agreement with KBC, of which US\$ 38.5 million had been utilized to repay previous debts with KBC. The facility bears LIBOR plus 5% and provides for 6-month grace period after which it has to be repaid by equal monthly installments over 30 months starting January 2003 by automatic withdrawals from the Company's account with KBC. This facility is collateralized by the Company's assets of US\$12.2 million, crude oil of 365,750 barrels valued at approximately US\$6.7 million and by sales proceeds under 36-month contract for the shipment of 15,000 barrels of oil per day. This loan was obtained for the purpose of financing capital expenditure and other purchases of production equipment.

In December 2000, the Company issued and registered 200,000 non-callable coupon bonds of US\$ 20 million (or 3,062 million tenge) with the National Securities Commission and Kazakh Stock Exchange. 62,145 bonds were placed at the end of 2000 and the remaining 137,855 were placed at the beginning of 2001 among various Pension Funds and Commercial Banks of Kazakhstan. The bonds bear interest at 11% per annum payable semi-annually and will mature in December 2003.

17. DEFERRED TAX LIABILITY

The Company is subject to corporate income tax at the prevailing statutory rate of 30%. Income tax expenses for the year ended December 31, 2002 and 2001 were as follows:

<i>In thousands of Kazakhstani tenge</i>	2002	2001
Income tax expenses comprises		
- current tax expense	3,735,170	581,143
- deferred tax expense	1,406,157	1,307,346
	5,141,327	1,888,489

Reconciliation between tax expense reported in the financial statements and income before taxes multiplied by the statutory rate of 30% for the year ended December 31, 2002 and 2001, is as follows:

<i>In thousands of Kazakhstani tenge</i>	2002	2001
Income before income tax	14,326,256	5,831,315
Statutory tax rate	30%	30%
Prima facie tax payable on accounting profit	4,297,877	1,749,395
Permanent accounting differences	843,450	139,094
Actual provision for income tax	5,141,327	1,888,489

Deferred income taxes are provided for the temporary differences between the financial statement and tax basis of the Company's assets and liabilities. As of December 31, 2002 and 2001, the Company's deferred net tax position comprised of the:

<i>In thousands of Kazakhstani tenge</i>	2002	2001
Liabilities arising from differences in:		
Property, plant and equipment	5,803,118	4,203,286
Other liabilities	94,343	288,018
Net deferred tax liability	5,897,461	4,491,304

NOTES TO THE FINANCIAL STATEMENTS (continued)

18. OTHER LONG-TERM LIABILITIES

Other long-term liabilities represent production based bonuses, which will be payable to the Government of Kazakhstan. Under the subsoil use contract the Company is required to pay production bonuses when cumulative production reaches certain levels. The first amount of production bonus of US\$1 million shall be paid when cumulative production reaches ten million tons from the date of the subsoil use contract. The production bonus payable is accrued under the unit-of-production basis. The Company accrued US\$530 thousand (82,312 thousand tenge) as of December 31, 2002 in relation to the first amount of production bonus.

19. FUTURE SITE RESTORATION AND ABANDONMENT RESERVE

The abandonment and site restoration liability has been recorded in the financial statements to reflect the cost of restoring well sites to their original condition. The cost has been estimated based on management's best estimates and available historic data.

As of December 31, 2002 and 2001 future site and abandonment provision comprised:

<i>In thousands of Kazakhstani tenge</i>	2002	2001
Liability as at January 1,	412,112	217,278
Additional provision	203,547	194,834
Liability as at December 31,	615,659	412,112

In accordance with the agreement with the Ministry of Energy, the Company has to accrue \$96,748 (14,812 thousand tenge) every month for the site restoration (liquidation) fund. The Company considers that this calculation is not adequate and actually provides \$110,569 (16,962 thousand tenge) on a monthly basis.

20. SHARE CAPITAL

Share capital consists of voting shares of nominal value 1,000 Tenge each. As at December 31, 2002 shareholders are as follows:

<i>In thousands of Kazakhstani tenge</i>	Number of shares	Par Value in tenge	Amount
Nations Energy Company Ltd. – common stock	2,045,035	1,000	2,045,035
Employees of the Company – preferred stock	116,027	1,000	116,027
	2,161,062		2,161,062

During 2002 the Company declared and paid dividends in total amount of 4,885,343 tenge for the first three quarters of 2002 on both common and preferred stock (2,261 tenge per share). Dividends payable on common stock in the amount of 4,622,965 thousand tenge were offset against the receivable due from the Parent. In January 2003 the Company declared 700 tenge per share on both common and preferred stock for the fourth quarter of 2002, which were offset in February against receivable due from the Parent.

Any dividend on shares is determined after consideration of the Company's profit, less income taxes and is a subject to approval by the Board of Directors.

Holders of the preferred stock are entitled to annual dividends of 20% of the nominal value of their shares regardless of the Company's profits. Preferred stock does not carry the right to vote.

NOTES TO THE FINANCIAL STATEMENTS (continued)**21. REVENUE**

The composition of revenue for the years ended December 31, 2002 and 2001 were as follows:

<i>In thousands of Kazakhstani tenge</i>	2002	2001
Export crude oil sales	34,115,493	15,867,853
Domestic crude oil sales	1,542,765	2,232,568
Royalty	(903,816)	(516,175)
	34,754,442	17,584,246

22. COST OF SALE

The composition of cost of sales for the years ended December 31, 2002 and 2001 were as follows:

<i>In thousands of Kazakhstani tenge</i>	2002	2001
Maintenance and repair	1,775,104	1,168,285
Field services (catering, security, housing, medical facility)	1,010,771	929,222
Salary and related benefits	1,007,176	766,911
Field supervision	623,146	435,280
Materials and supplies	449,698	362,170
Water supply	350,572	282,477
Electricity	377,469	224,142
Field Taxes	349,833	89,571
Gas	221,865	174,003
Other	151,867	82,275
	6,317,501	4,514,336

23. SELLING, GENERAL AND ADMINISTRATIVE EXPENSES

The composition of selling, general and administrative expenses for the years ended December 31, 2002 and 2001 were as follows:

<i>In thousands of Kazakhstani tenge</i>	2002	2001
Management fees (see Note 5)	2,284,725	1,802,826
Salary and related benefits	911,583	721,381
Consulting fees	219,158	166,837
Operating taxes	198,049	253,045
Social sphere and trainings	217,722	144,294
Insurance	171,792	62,165
Third parties services	179,085	165,810
Customs clearance and other selling expenses	151,924	84,697
Business trips	157,517	203,462
Bad debt provision	33,870	68,652
Other	58,924	4,301
	4,584,349	3,677,470

NOTES TO THE FINANCIAL STATEMENTS (continued)

24. FINANCIAL INSTRUMENTS

Credit Risk

Financial instruments, which potentially subject the Company to credit risk consists primarily of, accounts receivable. While the Company may be subject to losses up to the contract value of the instruments in the event of non-performance by its counterparts, it does not expect such losses to occur. No collateral is required by the Company to support financial instruments subject to credit risk.

The Company places its cash with high credit quality financial institutions.

Fair Values

The fair value of financial instruments, consisting of cash, receivables, payables and obligations under debt instruments, are considered to be equal to their carrying values. Adequate provisions are made in respect of accounts receivable. The fair values of the Company's investments are equivalent to the Company's share in the underlying net assets of the investee companies.

25. RELATED PARTIES TRANSACTIONS

During 2002 the Company paid to the Parent 2,284,725 thousand tenge (2001: 1,802,826 thousand tenge) for management fees. These fees relate to the costs being reimbursed to the Parent that had been incurred on behalf of the Company whilst performing management assistance, including marketing and administration services.

The Company started to rent a drilling rig and machine to the Parent's subsidiary, Tulpar Munai Service effective May 2002. Rent income from this operation in 2002 amounted to 194,662 thousand tenge (2001: nil). Tulpar Munai Service started to provide drilling services to the Company totaling 793,374 thousand tenge for 2002 (2001: nil).

Other transactions with related parties are disclosed in the Notes 5, 13 and 20.

26. CONTINGENT LIABILITIES

Current Economic Environment

In recent years, Kazakhstan has undergone substantial political and economic change. As an emerging market, Kazakhstan does not possess a well-developed business infrastructure, which generally exists in a more mature free market economy. As a result, operations carried out in Kazakhstan can involve significant risks, which are not typically associated with those in developed markets. Management is unable to estimate what changes may occur or the resulting effect of any such changes on the Group's financial condition or future results of operations.

Contingent Liabilities

The Company is party to various legal proceedings related to business operations, such as property damage claims and employee claims. The Company does not believe that pending or threatened claim of these types, individually or in aggregate, are likely to have any material adverse effect on the Company's financial position or results of operations.

The Company assesses the likelihood of material liabilities arising from individual circumstances and makes provision in its financial statements only where it is probable that actual events giving rise to liability will occur and the amount of the liability can be reasonably estimated. No provision has been made in these financial statements for any of the contingent liabilities mentioned above.

NOTES TO THE FINANCIAL STATEMENTS (continued)

26. CONTINGENT LIABILITIES (continued)

Taxation

Legislation and regulations regarding taxation, foreign currency translations and licensing of foreign currency loans in the Republic of Kazakhstan continue to evolve as the central government manages the transformation from a command to a market-oriented economy.

The various legislation and regulations are not always clearly written and their interpretation is subject to the opinions of the local tax inspectors, National Bank officials and the Ministry of Finance. Instances of inconsistent opinions between local, regional and national tax authorities and between National Bank and the Ministry of Finance are not unusual.

The current regime of penalties and interest related to reported and discovered violations of Kazakhstan's law, decrees and related regulations are severe. Penalties include confiscation of the amounts at issue (for currency law violations), as well as fines of generally 50% of the taxes unpaid. Interest is assessable at rates of generally 0.03% per day. As a result, penalties and interest can result in amounts that are multiples of any unreported taxes.

During 2002, the Company's books and records for 2001 and 2000 have been audited by the state tax authorities. In December 2002, as result of the tax audit, the Company received a claim from the Tax Committee of the Ministry of Finance of the Republic of Kazakhstan to pay additional taxes in the amount of 2,906,096 thousand tenge (US\$18.7 million) as well as penalties and fines totaling 447,323 thousand tenge (US\$2.9 million) (the "Tax Claim"). The Company's management believes that the Company is in compliance with the tax legislation and that the Tax Claim is disputable. The Company has appealed the Tax Claim to the Ministry of Finance and has contracted legal firm in Kazakhstan to assist with the appeal process. Based on the Company's management assessment of the Tax Claim, it is the Company's opinion that it will be successful in the appeal process. If the Company is unsuccessful in the appeal process, the Company may be required to take an appeal to the courts of Kazakhstan. The Company elected not to provide for the provision for the amounts of the Tax Claim as of December 31, 2002, since the appeal is in process and the final resolution of the Ministry of Finance has not been issued and management assessment this is only possible contingency.

The Company believes that it has paid or accrued all taxes that are applicable. Where practice concerning the provision of taxes is unclear, the Company has accrued tax liabilities based on management's best estimate. The Company's policy is to accrue contingencies in the accounting period in which a loss is deemed probable and the amount is reasonably determinable.

Because of the uncertainties associated with the Kazakh tax and legal systems, the ultimate amount of taxes, penalties and interest, if any, assessed may be in excess of the amount expensed to date and accrued at December 31, 2002. Although such amounts are possible and may be material, it is the opinion of the Company's management that these amounts are either not probable, not reasonably determinable, or both.

The Company's operations and financial position will continue to be affected by Kazakh political developments, including the application of existing and future legislation and tax regulations. The Company does not believe that these contingencies, as related to its operations, are any more significant than those of similar enterprises in Kazakhstan.

NOTES TO THE FINANCIAL STATEMENTS (continued)

26. CONTINGENT LIABILITIES (continued)**Environment**

The Company may also be subject to loss contingencies relating to regional environmental claims that may arise from the past operations of the related fields in which it operates. As Kazakh laws and regulations evolve concerning environmental assessments and site restoration, the Company may incur future costs, the amount of which is currently indeterminable due to such factors as the ultimate determination of responsible parties associated with these costs and the government's assessment of respective parties' ability to pay for the costs related to environmental reclamation. It is the opinion of management that such costs will not have a material effect on the financial condition of the Company and accordingly no provisions for future environmental claims or penalties are included in the accompanying financial statements.

However, depending on any unfavorable claims or penalties assessed by the Kazakh regulatory agencies, it is possible that the Company's future results of operations or cash flow could be materially affected in a particular period.

Governmental Influence, Pricing and Transportation Issues

The current political and economic situation in Kazakhstan is such that the Government, from time to time, attempts to influence oil producers to supply production to domestic refineries at prices that are substantially lower than prices for export sales. Prices for domestic sales have approximated 30-35% of world market prices during the year ended December 31, 2002.

Despite the fact that the Sale-Purchase Agreement between the Parent and Government provides that the Company will be entitled to compensation at world market prices for any forced domestic sales, management considers such volumes sold locally reasonable in terms of Kazakhstan's current economic situation. However, management is unable to predict what future actions may be taken by the Government to influence its future commercial operations and/or export sales.

The Company's oil production must be transported through pipelines owned by state oil transportation company KazTransOil ("KTO"). KTO has a monopoly on the transport market and as such, is able to directly impact transportation costs incurred by the Company as well as volumes of crude that the Company is able to export. As such, there is no assurance that the Company will be able to export all, or significant portions, of its production.

27. COMMITMENTS**Commitments under the License**

According to the subsoil use contract the Company is obliged to spend US\$250,000 annually for the training and educational programs for its employees. For the year ended December 31, 2002, the Company incurred US\$397,497 of training and educational expenses.

Guarantees Issued

At December 31, 2002 the Company had issued guarantees in favor of Kazakh banks for loans taken by its employees in the amount of US \$2,900 thousand (2001: US\$400 thousand).

Commitments under KBC loan

Under US\$65 million loan facility agreement with KBC (see Note 16) the Company is required to spend US\$50.6 million of capital investments since January 1, 2002 by the end of April 2003. As of December 31, 2002 the Company spent US\$41 million.